

**KAWASAKI HEAVY INDUSTRIES, LTD.**

# **Semiannual Report** 2006

For the six months ended September 30, 2006

# Consolidated Financial Highlights

Kawasaki Heavy Industries, Ltd. and Consolidated Subsidiaries  
For the six months ended September 30, 2006 and 2005

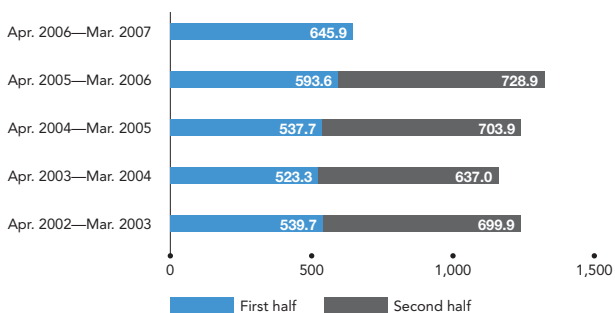
	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
<b>For the period:</b>			
Net sales.....	¥ 645,852	¥ 593,579	\$ 5,478,429
Operating income.....	25,562	12,577	216,829
Net income.....	11,414	5,233	96,819
Research and development expenses.....	14,300	11,200	121,300
Depreciation and amortization.....	14,879	14,384	126,211
Net cash provided by (used for) operating activities.....	(10,767)	11,216	(91,331)
<b>Per share (in yen and U.S. dollars):</b>			
Net income.....	¥ 7.33	¥ 3.63	\$ 0.06
Cash dividends.....	—	—	—
<b>At end of the period:</b>			
Total assets.....	¥1,319,100	¥1,193,901	\$11,189,244
Total shareholders' equity.....	244,170	207,499	2,071,168
<b>Orders received and outstanding:</b>			
Orders received during the period.....	¥ 763,844	¥ 516,694	\$ 6,479,294
Order backlog at end of the period.....	1,424,960	1,191,717	12,087,200
<b>Number of employees</b> .....	<b>29,461</b>	<b>29,024</b>	

Notes: 1. This semiannual report has been prepared in conformity with generally accepted accounting principles and practices in Japan.

2. All dollar figures herein refer to U.S. currency. Yen amounts have been translated, for convenience only, at ¥117.89 to \$1.00, the approximate rate of exchange at September 30, 2006.

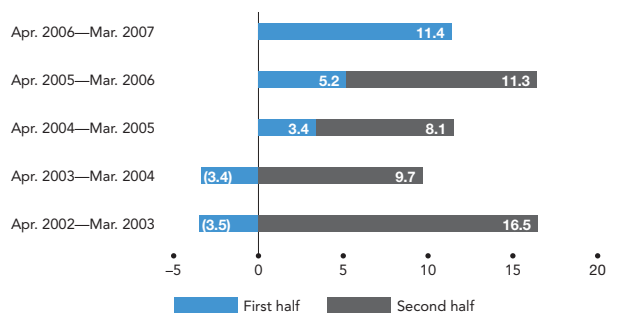
## Net Sales

(Billions of yen)



## Net Income (Loss)

(Billions of yen)



# To Our Shareholders

## New Medium-Term Business Plan "Global K" Targeting Before-Tax ROIC of 14% and Recurring Profit of ¥90 Billion

### Further Gains in Operating Income and Net Income

The Japanese economy continued on an expansionary trend during the interim period under review, ended September 30, 2006, propelled by growth in personal consumption and exports as well as by increases in private capital investment driven by an improvement in corporate earnings. Outside Japan, although some sectors in the U.S. economy slowed, the world economy continued to be generally strong, driven especially by expansion in Europe, China, and the rest of Asia.

Nevertheless, the operating environment for the Kawasaki Heavy Industries (KHI) Group continued to present challenges. Lackluster conditions prevailed in the domestic public works market, and prices of raw materials, such as steel and crude oil, remained at high levels, while prices of more costly materials, such as aluminum and titanium, rose sharply and shortages emerged.

Amid these conditions, the KHI Group maintained its proactive posture of confronting the challenges and aggressively pursuing market opportunities in the operating environment. As a consequence, the Group's net sales grew ¥52.3 billion, or 8.8% from the interim period of the previous year, to ¥645.9 billion, led especially by higher sales in the Aerospace and Consumer Products & Machinery segments.

Profitability showed further improvement, as a consequence of active measures to increase earnings in all aspects of the Group's operations. Operating income rose ¥13.0 billion, up 103.2% over the interim period of the previous year, to ¥25.6 billion. Net income for the period rose ¥6.2 billion, up 118.1%, to ¥11.4 billion.

Our basic policy is to pay dividends appropriate to earnings performance, while giving careful attention to increasing retained earnings. After giving due consideration to the uncertainties in the operating environment for the full fiscal year ending March 31, 2007, we have decided not to pay a cash dividend for the interim period under review.

### Preparation of a New Medium-Term Business Plan and Emphasis on Compliance

Under its previous medium-term business plan, which was based on the fundamental policy of "Quality Followed by Quantity," the KHI Group has exercised selectivity and focus in its allocation of resources. As a consequence, the Group has been able to restore the profitability of its activities, improve its financial position, and steadily improve the soundness of its business base. To move up to the next stage in growth and development, we have prepared a new medium-term business plan entitled "Global K." The new plan will begin in the current fiscal year and extend through the fiscal year ending March 31, 2011 and targets before-tax return on invested capital (ROIC)\*1 of 14% and recurring profit\*2 of ¥90 billion.

As we implement this new plan, we will be working to greatly improve the quality of our management activities. This will include strengthening our internal control systems, placing strong emphasis on compliance, and endeavoring to fulfill our responsibilities to society. With these goals in mind, in October 2006, we formed a specialized unit, the Corporate Social Responsibility (CSR) Department, which has the responsibility for driving our CSR activities.

The KHI Group is steadily implementing various policies to strengthen profitability in all its business activities and reform its business portfolio, with the objective of enhancing its corporate value. We would like to take this opportunity to ask you, our shareholders, for your renewed support and cooperation.

December 2006



Tadaharu Ohashi  
President

\*1, \*2 See page 6

# Medium-Term Business Plan “Global ”

## “Global Kawasaki”—The Next Exciting Stage

KHI’s new Medium-Term Business Plan “Global K” will begin in fiscal 2007, ending March 31, 2007, and extend through fiscal 2011. The first step in preparing this plan was to create a vision for the KHI Group and each of its business domains a decade into the future. Looking toward this vision of the future, KHI then developed this medium-term plan for growth for the next five years. The plan will be revised as necessary in fiscal 2009.

### 1. CORPORATE VISION

## Enriching Lifestyles and Helping Safeguard the Environment: **Global Kawasaki**

KHI aims to become a leading global enterprise that enriches lifestyles and helps safeguard the environment through its businesses, which encompass land, sea and air transportation systems, as well as the energy and environmental engineering sectors.

### What Each Business Should Be 10 Years in the Future

#### **Rolling Stock**

A world-class maker of rolling stock systems that draws on leading-edge technologies and feature top quality

#### **Aerospace**

A leader in Japan’s aerospace industry, with solid competitiveness internationally in aircraft manufacturing

#### **Gas Turbines & Machinery**

A prime mover manufacturer with world-class technologies in the transportation equipment and energy fields

#### **Consumer Products & Machinery**

A leisure vehicle and engine manufacturer with a top brand recognized for high quality and high performance

#### **Energy & Environmental Engineering**

A global leader in energy and environmental engineering with a reputation built on superb, proprietary technologies

#### **Industrial Robots**

A world-leading industrial robot manufacturer with a reputation built on key and systems technologies for high-performance and multifunctional robots

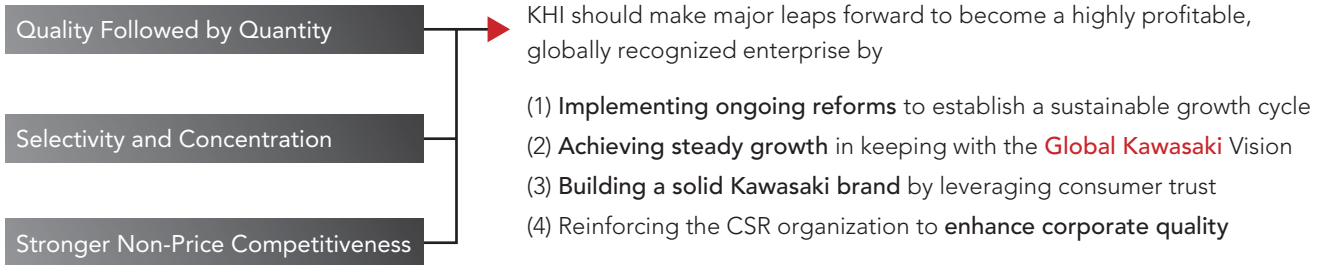
#### **Shipbuilding**

A shipbuilder with world-class profitability that draws on advanced technologies and a production site in China to withstand market swings

#### **Industrial Hydraulic Products**

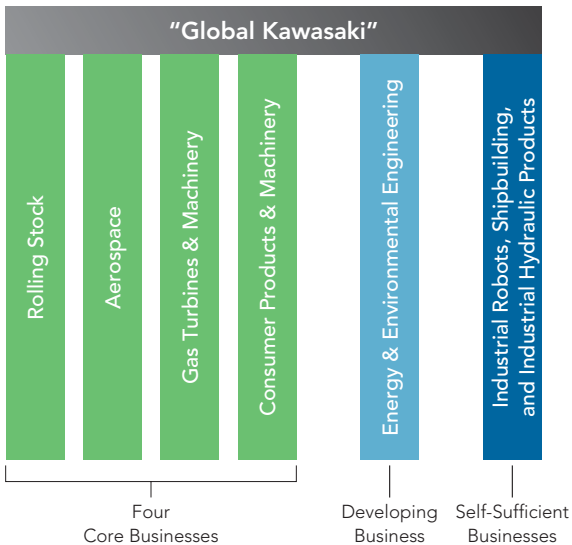
One of the world’s top five hydraulic equipment manufacturers, with outstanding technologies and product quality

## 2. BASIC OBJECTIVES



## 3. SELECTIVITY AND CONCENTRATION

### 1. Positioning of KHI Businesses



#### Four Core Businesses

Rolling Stock, Aerospace, Gas Turbines & Machinery, and Consumer Products & Machinery

Should be operating globally as earnings drivers of the KHI Group

#### Developing Business

##### Energy & Environmental Engineering

(Redirecting the Plant & Infrastructure Engineering business toward energy-related and environmental-related activities to achieve further growth and development)

Should be nurtured as a new earnings driver of the Group by implementing various measures, including redirection of businesses and M&A

#### Self-Sufficient Businesses

Industrial Robots, Shipbuilding, and Industrial Hydraulic Products

Should establish a position as a specialist in each business field and secure stable earnings

## 2. Positioning of Business Units/Products

	Priority Businesses Will drive sustainable growth. Expand earnings through focused investments	Developing Businesses Strengthen competitiveness through focused investments	Businesses with Stable Earnings Achieve consistent returns	Businesses Requiring Structural Reform
Rolling Stock	Railcars for overseas markets	Railway systems Gigacell-powered LRVs	Railcars for Japanese market	Policies will be decided going forward and focus will be on public-sector investment related areas in Japan.
Aerospace	Defense aircraft Commercial aircraft	Convert P-X and C-X to commercial aviation use Commercial helicopters	Guidance systems	
Gas Turbines & Machinery	Engines for commercial aircraft	Gas turbine power generation systems Gas engines	Engines for defense sector (for aircraft and ships) Steam turbines for marine and industrial applications Aerodynamic machinery	
Consumer Products & Machinery	Motorcycles for industrialized markets	Motorcycles for industrializing markets	General-purpose gasoline engines	
Energy & Environmental Engineering		Gigacells® Biomass power generation systems Treatment of harmful substances LNG tanks Energy and environment related facilities	Industrial plants	
Industrial Robots		Industrial robots		
Shipbuilding	Merchant vessels (production in China)		Naval vessels Merchant vessels (production in Kobe and Sakaide)	
Industrial Hydraulic Products	For construction machinery		For industrial equipment and ships	

Note: Meaning of terms highlighted in red, which indicate new products under development, are as follows: (a) Gigacells®: Nickel-metal hydride batteries, (b) LRV: Light rail vehicle, tram car with super-low floor, (c) P-X: Next maritime patrol aircraft, (d) P-X: Next transport aircraft

## 4. PLANS FOR ALLOCATION OF MANAGEMENT RESOURCES

KHI will place emphasis on allocating management resources to priority businesses and developing businesses to ensure future growth.

### Capital investment plan

- ▶ Invest ¥300 billion over five years, or ¥60 billion annually  
(This compares with an average of ¥47 billion over the past three years.)

### R&D investment plan

- ▶ Invest ¥200 billion over five years, or ¥40 billion annually  
(This compares with an average of ¥27 billion over the past three years.)

### Personnel plan

- ▶ To compensate for the increased number of employees reaching mandatory retirement age and to facilitate implementation of KHI's expansion plans, KHI will hire 5,000 new staff over five years, or 1,000 people annually. This will result in an estimated increase in the number of employees to 31,000 at the end of fiscal 2011, 2,000 higher than at the end of fiscal 2006.

## 5. PRIORITY INITIATIVES

### 1) Strengthen technological capabilities

With renewed awareness that technology is a key source of earnings, reinforce technological development capabilities, production technology capabilities, and intellectual asset strategies.

### 2) Encourage market-oriented thinking and action

Become more market-focused to strengthen non-price competitiveness. Keep in mind that profits are generated from the market. All thinking and action in all processes of business operations should stem from the market.

### 3) Accelerate global business development

Aimed at future growth, accelerate global business development in sales, production, and procurement, while cooperating with partner companies.

### 4) Create and cultivate new products and business

Cultivate next-generation core businesses throughout the duration of the Global K plan by upgrading technologies and creating new businesses fulfilling high-priority social needs.

### 5) Strengthen Group management capabilities

While maintaining the advantages of the internal company system of management efficiency and flexibility, reinforce the Companywide strategy development and Group management/oversight functions at headquarters aimed at increasing the centripetal force of the KHI Group and harmonizing the optimization of the Company's individual parts and the Group as a whole.

Create a smaller, strong, and more agile headquarters and selectively reinforce the operations of subsidiaries and affiliates.

### 6) Promote Corporate Social Responsibility (CSR)

Improve management quality by promoting CSR with a focus on enhancing internal control systems and compliance, increase management transparency (commitment and accountability), strengthen risk management capabilities, and conduct environment-friendly business operations.

## 6. QUANTITATIVE TARGETS

- Strengthen profitability
- Reinforce financial position

- Increase ROIC
- Increase the ratio of recurring profit to net sales

### Targets for Fiscal 2011

- Before-tax ROIC\*<sup>1</sup>: 14%
- Recurring profit\*<sup>2</sup> to net sales ratio: 5.8%
- Net sales: ¥1,560 billion
- Operating income: ¥100 billion
- Recurring profit: ¥90 billion
- Debt-to-equity ratio\*<sup>3</sup>: 100% or less
- Shareholders' equity ratio: 30% or more

\*1: Before-tax ROIC: Earnings before interest and taxes (EBIT) divided by invested capital

\*2: Recurring profit is used in accounting standards generally accepted in Japan. It is the sum of operating income, net interest income (expenses), dividend income, and other non-operating but recurring items.

\*3: Debt-to-equity ratio: Ratio of interest-bearing debt to total shareholders' equity

**Policy for Shareholder Return:** Gradually increase dividends in line with improvement in profitability. Set a medium- to long-term target payout ratio of 30%, with dividends set based on financial projections and the progress toward the implementation of the business plan.

### Cautionary Statement

The performance outlook and forecasts stated in these materials were prepared by Kawasaki Heavy Industries, Ltd. (hereinafter, KHI), based on the circumstances as of the release date, and include potential risks and uncertain factors that relate to economic conditions, foreign currency exchange rates, tax rules, regulations, and other factors. Accordingly, please note that the actual operating results, financial position, and business development of KHI may sometimes differ considerably from the descriptions in the present projections.



Enriching lifestyles and helping safeguard the environment

"Global Kawasaki"





# Review of Operations

## Shipbuilding

This segment secured orders amounting to ¥69.5 billion, ¥31.0 billion, or 80.7% higher than in the same period of the previous year. Orders were obtained for 10 new vessels in total: one LNG carrier, seven bulk carriers, and two LPG carriers. This compared to orders a year earlier for three new vessels in total: two LNG carriers and one LPG carrier.

Sales showed a decline of ¥11.6 billion, down 21.6%, to ¥42.1 billion, due to lower sales of newbuildings. The segment reported an operating loss of ¥2.1 billion, mainly because of increases in prices of materials.



## Rolling Stock & Construction Machinery

This segment continued to secure large orders for commuter train cars from North America. As a result, orders leaped ¥78.4 billion, or 101.0%, to ¥156.1 billion.

Operating income climbed ¥3.9 billion, up 171.1%, to ¥6.1 billion, owing to an improvement in the profitability of overseas projects.

Sales were up ¥2.6 billion, or 3.1%, to ¥86.9 billion. Although sales of rolling stock in Japan decreased, deliveries for overseas customers, including the Taiwan High Speed Rail Corporation increased.



## Aerospace

Orders received increased ¥20.8 billion, or 42.1%, to ¥70.2 billion, because of higher demand from the commercial aircraft sector, principally orders from The Boeing Company for component parts for the Boeing 777 passenger aircraft.

next maritime patrol aircraft and C-X next transport aircraft for the Japan Defense Agency, an increase in sales of component parts for the Boeing 777 passenger aircraft, and other factors. Operating income declined ¥0.5 billion, or 9.0%, to ¥5.1 billion, owing to the adverse impact of higher material costs.



## Gas Turbines & Machinery

Orders won by this segment increased ¥2.2 billion, or 2.2%, to ¥99.3 billion, as a consequence of higher demand for industrial gas turbines and other factors.

Sales climbed ¥11.4 billion, or 16.5%, to ¥80.5 billion, mainly due to an increase

in sales for component parts for jet engines for commercial aircraft.

Operating income rose a marked ¥3.5 billion, up 258.4%, to ¥4.8 billion, driven by growth in sales, favorable movements in foreign exchange rates, and other factors.



## Plant & Infrastructure Engineering

This segment reported a sharp rise in orders of ¥68.8 billion, up 261.8%, to ¥95.1 billion, on the strength of major orders from overseas customers. These included a cement plant in Vietnam and a ferronickel plant in Korea.

Sales declined ¥16.5 billion, down 24.0%, to ¥52.1 billion, owing to a decline in sales of plants ordered

previously by overseas customers. This segment reported an operating loss of ¥3.7 billion, which was a ¥1.9 billion improvement from a larger operating loss in the same period of the previous fiscal year, owing to better operating results in the industrial plant business.



## Consumer Products & Machinery

Sales increased ¥23.6 billion, up 14.2%, to ¥189.9 billion, boosted by higher revenues generated from motorcycles in North America and Europe. Operating income rose sharply by ¥5.8 billion, up 112.0%, to ¥10.9 billion, supported by expansion in profits of the industrial

robot business and the favorable impact of movements in foreign exchange rates.



## Other

Sales came to ¥79.8 billion, a gain of ¥19.6 billion, or 32.6%, over the same period of the previous fiscal year, as sales of the hydraulic machinery business

to customers in China increased. Operating income climbed ¥1.4 billion, up 47.5%, to ¥4.4 billion.



## Review by Geographic Segment

Sales in Japan rose ¥14.6 billion, up 3.3% in comparison with the interim period of the previous year, to ¥459.8 billion, mainly because of an increase in sales of the parent company. Operating income climbed ¥9.9 billion, up 92.5%, to ¥20.5 billion.

In North America, sales jumped ¥22.4 billion, up 23.0%, to ¥119.6 billion, boosted by robust sales of motorcycles and other factors. Operating income rose ¥0.8 billion, up 345.0%, to ¥1.1 billion.

Sales in Europe expanded ¥14.4 billion, up 39.2%, to ¥51.0 billion, because of strong sales of motorcycles in this region. Operating income rose ¥1.1 billion, up 155.8%, to ¥1.8 billion.

## Financial Position

Total assets at the end of the interim period were ¥1,319.1 billion, ¥35.0 billion higher than at the end of the previous fiscal year (ended March 31, 2006), mainly because of an increase in inventories accompanying the rise in orders. Interest-bearing debt rose ¥29.9 billion, to ¥349.7 billion, accompanying the increase in the scale of the Group's operations.

Among cash flows, net cash flows from operating activities amounted to a net outflow of ¥10.8 billion, primarily as a consequence of the previously mentioned increase in inventories, compared with a net inflow of ¥11.2 billion in the same period of the previous fiscal year.

Net cash used for investing activities amounted to ¥26.7 billion, reflecting capital expenditures and other factors, compared with a net outflow of ¥7.7 billion in the same

In Asia, sales declined ¥2.1 billion, down 18.9%, to ¥9.2 billion, owing to lower sales of motorcycles in Indonesia and other factors. Operating income dropped ¥0.3 billion, or 43.9%, to ¥0.4 billion.

In other areas, sales grew ¥3.0 billion, up 93.5%, to ¥6.3 billion, while operating income amounted to ¥0.1 billion, an improvement from an operating loss of ¥0.2 billion for the same period a year earlier.

period of the previous fiscal year. As a result, free cash flow amounted to a net outflow of ¥37.5 billion.

Net cash provided by financing activities amounted to ¥24.8 billion, due mainly to an increase in short-term borrowings which was partially offset by an increase in the repayment of corporate bonds. This compared with a net outflow of ¥15.5 billion in the same period of the previous fiscal year.

As a result of these movements in cash flows, cash and cash equivalents at the end of the interim period under review were ¥24.9 billion, ¥12.6 billion lower than at the end of the previous fiscal year.

# Condensed Consolidated Balance Sheets

Kawasaki Heavy Industries, Ltd. and Consolidated Subsidiaries  
As of September 30 and March 31, 2006 and September 30, 2005

	Millions of yen			Thousands of U.S. dollars
	September 30, 2006 (unaudited)	March 31, 2006	September 30, 2005 (unaudited)	September 30, 2006 (unaudited)
<b>Assets:</b>				
Current assets:				
Cash on hand and in banks.....	¥ 25,006	¥ 37,650	¥ 32,685	\$ 212,113
Receivables, less allowance .....	429,542	438,204	375,420	3,643,583
Inventories.....	425,754	383,017	375,367	3,611,451
Other current assets .....	57,832	57,028	53,533	490,559
Total current assets .....	<u>938,134</u>	<u>915,899</u>	<u>837,005</u>	<u>7,957,706</u>
Investments and long-term loans, less allowance .....	86,015	76,757	84,250	729,621
Net property, plant and equipment.....	249,200	246,219	239,731	2,113,835
Intangible and other assets .....	45,751	45,210	32,915	388,082
Total assets.....	<u>¥1,319,100</u>	<u>¥1,284,085</u>	<u>¥1,193,901</u>	<u>\$11,189,244</u>
<b>Liabilities and shareholders' equity:</b>				
Current liabilities:				
Short-term borrowings and current portion of long-term debt.....	¥ 182,746	¥ 162,746	¥ 145,614	\$ 1,550,140
Payables.....	404,909	409,942	331,495	3,434,634
Advances from customers.....	111,846	98,590	132,533	948,732
Other current liabilities.....	122,631	131,381	91,006	1,040,215
Total current liabilities.....	<u>822,132</u>	<u>802,659</u>	<u>700,648</u>	<u>6,973,721</u>
Long-term liabilities:				
Long-term debt, less current portion.....	167,003	157,057	194,296	1,416,600
Others.....	85,795	81,273	86,601	727,755
Total long-term liabilities.....	<u>252,798</u>	<u>238,330</u>	<u>280,897</u>	<u>2,144,355</u>
Minority interests .....	—	5,508	4,857	—
Shareholders' equity:				
Common stock.....	92,106	92,085	81,427	781,288
Capital surplus .....	42,110	42,094	31,390	357,197
Retained earnings.....	107,457	100,776	90,135	911,502
Net unrealized gains on securities .....	12,720	14,097	19,155	107,897
Gain (loss) on hedging items .....	(3,698)	—	—	(31,368)
Foreign currency translation adjustments .....	(11,620)	(11,426)	(14,467)	(98,566)
Treasury stock .....	(43)	(38)	(141)	(365)
Minority interests .....	5,138	—	—	43,583
Total shareholders' equity .....	<u>244,170</u>	<u>237,588</u>	<u>207,499</u>	<u>2,071,168</u>
Total liabilities and shareholders' equity.....	<u>¥1,319,100</u>	<u>¥1,284,085</u>	<u>¥1,193,901</u>	<u>\$11,189,244</u>

# Condensed Consolidated Statements of Operations and Retained Earnings

Kawasaki Heavy Industries, Ltd. and Consolidated Subsidiaries  
For the six months ended September 30, 2006 and 2005 (unaudited)

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
Net sales .....	<b>¥645,852</b>	¥593,579	<b>\$5,478,429</b>
Cost of sales .....	<b>555,715</b>	518,619	<b>4,713,843</b>
Gross profit.....	<b>90,137</b>	74,960	<b>764,586</b>
Selling, general and administrative expenses.....	<b>64,575</b>	62,383	<b>547,757</b>
Operating income .....	<b>25,562</b>	12,577	<b>216,829</b>
Other income (expenses):			
Interest and dividend income.....	<b>1,891</b>	2,014	<b>16,040</b>
Equity in income of unconsolidated subsidiaries and affiliates.....	<b>855</b>	(103)	<b>7,253</b>
Interest expense .....	<b>(2,912)</b>	(2,678)	<b>(24,701)</b>
Other, net.....	<b>(5,156)</b>	(3,617)	<b>(43,736)</b>
Income before income taxes and minority interests .....	<b>20,240</b>	8,193	<b>171,685</b>
Income taxes .....	<b>(8,577)</b>	(2,832)	<b>(72,754)</b>
Minority interests in net income of consolidated subsidiaries .....	<b>(249)</b>	(128)	<b>(2,112)</b>
Net income.....	<b>¥ 11,414</b>	¥ 5,233	<b>\$ 96,819</b>
Retained earnings:			
Balance at beginning of the period .....	¥ —	¥ 88,704	\$ —
Net income for the period .....	—	5,233	—
Cash dividends.....	—	(3,606)	—
Bonuses to directors and statutory auditors .....	—	(84)	—
Reduction due to change of consolidation period of subsidiaries .....	—	—	—
Other.....	—	(112)	—
Balance at end of the period .....	<b>¥ —</b>	<b>¥ 90,135</b>	<b>\$ —</b>

# Condensed Consolidated Statements of Cash Flows

Kawasaki Heavy Industries, Ltd. and Consolidated Subsidiaries  
For the six months ended September 30, 2006 and 2005 (unaudited)

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
<b>Cash flows from operating activities:</b>			
Income before income taxes and minority interests .....	¥20,240	¥ 8,193	\$ 171,685
Adjustments to reconcile net income before income taxes and minority interests to net cash provided by operating activities:			
Depreciation and amortization.....	14,879	14,384	126,211
Increase in assets .....	(34,449)	(6,771)	(292,213)
Increase in liabilities.....	12,935	2,150	109,721
Other.....	(24,372)	(6,740)	(206,735)
<b>Net cash provided by (used for) operating activities.....</b>	<b>(10,767)</b>	<b>11,216</b>	<b>(91,331)</b>
<b>Cash flows from investing activities:</b>			
Acquisition of tangible and intangible assets .....	(15,909)	(15,305)	(134,948)
Acquisition of investments in securities.....	(11,850)	(425)	(100,517)
Other.....	1,024	8,038	8,686
<b>Net cash used for investing activities.....</b>	<b>(26,735)</b>	<b>(7,692)</b>	<b>(226,779)</b>
<b>Cash flows from financing activities:</b>			
Increase (Decrease) in short-term borrowings .....	39,513	(4,055)	335,168
Proceeds from long-term debt.....	18,355	15,503	155,696
Repayment of long-term debt.....	(28,289)	(23,189)	(239,961)
Other.....	(4,807)	(3,717)	(40,775)
<b>Net cash provided by (used for) financing activities .....</b>	<b>24,772</b>	<b>(15,458)</b>	<b>210,128</b>
<b>Effect of exchange rate changes.....</b>	<b>118</b>	<b>173</b>	<b>1,001</b>
<b>Net decrease in cash and cash equivalents.....</b>	<b>(12,612)</b>	<b>(11,761)</b>	<b>(106,981)</b>
<b>Cash and cash equivalents at beginning of the period.....</b>	<b>37,506</b>	<b>44,385</b>	<b>318,144</b>
<b>Decrease in cash and cash equivalents arising from exclusion of consolidated subsidiaries.....</b>	<b>—</b>	<b>(111)</b>	<b>—</b>
<b>Cash and cash equivalents at end of the period.....</b>	<b>¥24,894</b>	<b>¥32,513</b>	<b>\$ 211,163</b>

# Consolidated Statements of Shareholders' Equity

Kawasaki Heavy Industries, Ltd. and Consolidated Subsidiaries  
For the six months ended September 30, 2006 (unaudited)

	Thousands	Millions of yen							
	Number of shares of common stock	2006							
		Common stock	Capital surplus	Retained earnings	Net unrealized gains on securities	Gain (loss) on hedging items	Foreign currency translation adjustments	Treasury stock	Minority interests
Balance at March 31, 2006.....	1,557,715	¥92,085	¥42,094	¥100,776	¥14,097	¥ —	¥(11,426)	¥(38)	¥5,508
Net income for the interim period.....	—	—	—	11,414	—	—	—	—	—
Issue of new shares.....	224	21	15	—	—	—	—	—	—
Cash dividends .....	—	—	—	(4,673)	—	—	—	—	—
Treasury stock purchased, net.....	—	—	1	—	—	—	—	(5)	—
Bonuses to directors and statutory auditors.....	—	—	—	(14)	—	—	—	—	—
Other .....	—	—	—	(46)	(1,377)	(3,698)	(194)	—	(370)
<b>Balance at September 30, 2006 .....</b>	<b>1,557,939</b>	<b>¥92,106</b>	<b>¥42,110</b>	<b>¥107,457</b>	<b>¥12,720</b>	<b>¥(3,698)</b>	<b>¥(11,620)</b>	<b>¥(43)</b>	<b>¥5,138</b>

	Thousands of U.S. dollars							
	2006							
	Common stock	Capital surplus	Retained earnings	Net unrealized gains on securities	Gain (loss) on hedging items	Foreign currency translation adjustments	Treasury stock	Minority interests
Balance at March 31, 2006 .....	\$781,110	\$357,062	\$854,831	\$119,578	\$ —	\$(96,921)	\$(322)	\$46,722
Net income for the interim period .....	—	—	96,819	—	—	—	—	—
Issue of new shares .....	178	127	—	—	—	—	—	—
Cash dividends.....	—	—	(39,639)	—	—	—	—	—
Treasury stock purchased, net.....	—	8	—	—	—	—	(42)	—
Bonuses to directors and statutory auditors .....	—	—	(119)	—	—	—	—	—
Other .....	—	—	(390)	(11,680)	(31,368)	(1,646)	—	(3,139)
<b>Balance at September 30, 2006.....</b>	<b>\$781,288</b>	<b>\$357,197</b>	<b>\$911,502</b>	<b>\$107,897</b>	<b>\$(31,368)</b>	<b>\$(98,566)</b>	<b>\$(365)</b>	<b>\$43,583</b>

# Segment Information

Kawasaki Heavy Industries, Ltd. and Consolidated Subsidiaries  
For the six months ended September 30, 2006 and 2005 (unaudited)

## (a) Information by industry segment

	Millions of yen				
	2006				
	External sales	Intersegment sales	Total sales	Operating expenses	Operating income (loss)
Shipbuilding .....	¥ 42,107	¥ 1,296	¥ 43,403	¥ 45,456	¥ (2,053)
Rolling Stock & Construction Machinery .....	86,925	260	87,185	81,040	6,145
Aerospace .....	114,452	614	115,066	109,968	5,098
Gas Turbines & Machinery .....	80,509	7,941	88,450	83,629	4,821
Plant & Infrastructure Engineering .....	52,114	9,068	61,182	64,910	(3,728)
Consumer Products & Machinery .....	189,928	4,318	194,246	183,342	10,904
Other .....	79,817	20,224	100,041	95,611	4,430
Total .....	645,852	43,721	689,573	663,956	25,617
Eliminations .....	—	(43,721)	(43,721)	(43,666)	(55)
Consolidated total .....	¥645,852	¥ —	¥645,852	¥620,290	¥25,562

	Millions of yen				
	2005				
	External sales	Intersegment sales	Total sales	Operating expenses	Operating income (loss)
Shipbuilding .....	¥ 53,736	¥ 589	¥ 54,325	¥ 53,561	¥ 764
Rolling Stock & Construction Machinery .....	84,331	465	84,796	82,529	2,267
Aerospace .....	91,293	951	92,244	86,643	5,601
Gas Turbines & Machinery .....	69,093	7,150	76,243	74,898	1,345
Plant & Infrastructure Engineering .....	68,609	6,121	74,730	80,395	(5,665)
Consumer Products & Machinery .....	166,339	2,295	168,634	163,490	5,144
Other .....	60,178	21,846	82,024	79,021	3,003
Total .....	593,579	39,417	632,996	620,537	12,459
Eliminations .....	—	(39,417)	(39,417)	(39,535)	118
Consolidated total .....	¥593,579	¥ —	¥593,579	¥581,002	¥12,577

	Thousands of U.S. dollars				
	2006				
	External sales	Intersegment sales	Total sales	Operating expenses	Operating income (loss)
Shipbuilding .....	\$ 357,172	\$ 10,993	\$ 368,165	\$ 385,580	\$ (17,415)
Rolling Stock & Construction Machinery .....	737,340	2,205	739,545	687,420	52,125
Aerospace .....	970,837	5,208	976,045	932,802	43,243
Gas Turbines & Machinery .....	682,916	67,360	750,276	709,382	40,894
Plant & Infrastructure Engineering .....	442,056	76,919	518,975	550,598	(31,623)
Consumer Products & Machinery .....	1,611,061	36,628	1,647,689	1,555,195	92,494
Other .....	677,047	171,550	848,597	811,019	37,578
Total .....	5,478,429	370,863	5,849,292	5,631,996	217,296
Eliminations .....	—	(370,863)	(370,863)	(370,396)	(467)
Consolidated total .....	\$5,478,429	\$ —	\$5,478,429	\$5,261,600	\$216,829



**(b) Information by geographic area**

	Millions of yen				
	2006				
	External sales	Intersegment sales	Total sales	Operating expenses	Operating income
Japan.....	¥459,768	¥ 120,560	¥580,328	¥559,793	¥20,535
North America.....	119,598	8,130	127,728	126,669	1,059
Europe.....	51,015	2,049	53,064	51,291	1,773
Asia.....	9,171	8,685	17,856	17,447	409
Other areas.....	6,300	77	6,377	6,254	123
Total.....	645,852	139,501	785,353	761,454	23,899
Eliminations.....	—	(139,501)	(139,501)	(141,164)	1,663
Consolidated total.....	¥645,852	¥ —	¥645,852	¥620,290	¥25,562

	Millions of yen				
	2005				
	External sales	Intersegment sales	Total sales	Operating expenses	Operating income
Japan.....	¥445,137	¥ 99,957	¥545,094	¥534,427	¥10,667
North America.....	97,241	6,997	104,238	104,000	238
Europe.....	36,638	1,888	38,526	37,833	693
Asia.....	11,307	8,708	20,015	19,286	729
Other areas.....	3,256	54	3,310	3,479	(169)
Total.....	593,579	117,604	711,183	699,025	12,158
Eliminations.....	—	(117,604)	(117,604)	(118,023)	419
Consolidated total.....	¥593,579	¥ —	¥593,579	¥581,002	¥12,577

	Thousands of U.S. dollars				
	2006				
	External sales	Intersegment sales	Total sales	Operating expenses	Operating income
Japan.....	\$3,899,975	\$1,022,648	\$4,922,623	\$4,748,435	\$174,188
North America.....	1,014,488	68,963	1,083,451	1,074,468	8,983
Europe.....	432,734	17,381	450,115	435,075	15,040
Asia.....	77,793	73,670	151,463	147,994	3,469
Other areas.....	53,439	653	54,092	53,049	1,043
Total.....	5,478,429	1,183,315	6,661,744	6,459,021	202,723
Eliminations.....	—	(1,183,315)	(1,183,315)	(1,197,421)	14,106
Consolidated total.....	\$5,478,429	\$ —	\$5,478,429	\$5,261,600	\$216,829

(c) Overseas sales

	Millions of yen		Millions of yen		Thousands of
		%		%	U.S. dollars
	<b>2006</b>		2005		<b>2006</b>
	Overseas sales	% of net sales	Overseas sales	% of net sales	Overseas sales
North America .....	<b>¥155,019</b>	<b>24.0%</b>	¥125,730	21.2%	<b>\$1,314,946</b>
Europe .....	<b>57,932</b>	<b>8.9</b>	51,991	8.8	<b>491,407</b>
Asia .....	<b>96,354</b>	<b>15.0</b>	105,594	17.8	<b>817,321</b>
Other areas .....	<b>60,221</b>	<b>9.3</b>	46,077	7.7	<b>510,824</b>
Total.....	<b>¥369,526</b>	<b>57.2%</b>	¥329,392	55.5%	<b>\$3,134,498</b>

## Changes in Accounting Policies

Effective April 1, 2006, Kawasaki Heavy Industries, Ltd., and its consolidated subsidiaries adopted a new accounting standard for "Presentation of Net Assets in the Balance Sheet" issued by the Accounting Standards Board of Japan. As a result of adopting the standard, "Minority interests" and "Gain (loss) on hedging items" are presented in Shareholders' equity.

# Net Sales, Orders and Order Backlog by Industry Segment

For the six months ended September 30, 2006 and 2005 (unaudited)

	Millions of yen		Thousands of U.S. dollars
	2006	2005	2006
<b>Net sales:</b>			
Shipbuilding.....	¥ 42,107	¥ 53,736	\$ 357,172
Rolling Stock & Construction Machinery.....	86,925	84,331	737,340
Aerospace.....	114,452	91,293	970,837
Gas Turbines & Machinery.....	80,509	69,093	682,916
Plant & Infrastructure Engineering.....	52,114	68,609	442,056
Consumer Products & Machinery.....	189,928	166,339	1,611,061
Other.....	79,817	60,178	677,047
Total.....	<b>¥645,852</b>	<b>¥593,579</b>	<b>\$5,478,429</b>

## Orders received:

Shipbuilding.....	¥ 69,507	¥ 38,469	\$ 589,592
Rolling Stock & Construction Machinery.....	156,102	77,678	1,324,133
Aerospace.....	70,175	49,371	595,258
Gas Turbines & Machinery.....	99,313	97,161	842,421
Plant & Infrastructure Engineering.....	95,093	26,285	806,625
Consumer Products & Machinery.....	189,928	166,339	1,611,061
Other.....	83,726	61,391	710,204
Total.....	<b>¥763,844</b>	<b>¥516,694</b>	<b>\$6,479,294</b>

	Millions of yen			Thousands of U.S. dollars
	As of September 30, 2006	As of March 31, 2006	As of September 30, 2005	As of September 30, 2006

## Order backlog:

Shipbuilding.....	¥ 315,263	¥ 289,227	¥ 252,825	\$ 2,674,213
Rolling Stock & Construction Machinery.....	412,985	346,310	297,326	3,503,139
Aerospace.....	256,954	301,599	247,671	2,179,608
Gas Turbines & Machinery.....	214,002	195,108	194,754	1,815,268
Plant & Infrastructure Engineering.....	187,030	144,147	169,345	1,586,479
Consumer Products & Machinery.....	—	—	—	—
Other.....	38,726	34,053	29,796	328,493
Total.....	<b>¥1,424,960</b>	<b>¥1,310,444</b>	<b>¥1,191,717</b>	<b>\$12,087,200</b>



## Kawasaki Corporate Data

(As of September 30, 2006)

### Kawasaki Heavy Industries, Ltd.

#### Kobe Head Office:

Kobe Crystal Tower,  
1-3, Higashikawasaki-cho 1-chome,  
Chuo-ku, Kobe, Hyogo 650-8680, Japan

#### Tokyo Head Office:

World Trade Center Bldg.,  
4-1, Hamamatsu-cho 2-chome,  
Minato-ku, Tokyo 105-6116, Japan

**Founded:** 1878

**Incorporated:** 1896

**Paid-in Capital:** ¥92,106,094,655

**Number of Shares Issued:** 1,557,939,285

**Number of Shareholders:** 153,691

**Number of Employees:** 29,461

#### Stock Exchange Listings:

Tokyo, Osaka, Nagoya

#### Newspaper in Which Public Notices Are Made:

*Nihon Keizai Shimbun*

#### Transfer Agent:

The Chuo Mitsui Trust and Banking Company, Limited  
33-1, Shiba 3-chome,  
Minato-ku, Tokyo 105-8574, Japan

#### Handling Office:

The Chuo Mitsui Trust and Banking Company, Limited  
Osaka Branch Office  
2-21, Kitahama 2-chome,  
Chuo-ku, Osaka 541-0041, Japan

#### Independent Auditors:

KPMG AZSA & Co.  
Kobe Crystal Tower,  
1-3, Higashikawasaki-cho 1-chome,  
Chuo-ku, Kobe, Hyogo 650-8680, Japan

#### ADR Facility:

KHI has a sponsored American Depository Receipt (ADR) facility. ADRs are traded in the over-the-counter (OTC) market in the United States under CUSIP number 486 359 20 1 with each ADR representing four ordinary shares.

#### ADR Depository:

The Bank of New York  
101 Barclay St., 22 West,  
New York, NY 10286, U.S.A.  
Phone: 1-212-815-2042  
U.S. Toll Free: 888-269-2377  
(888-BNY-ADRS)  
<http://adrbny.com>

KHI Web Site at: <http://www.khi.co.jp>



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